

SECTION 1: EXECUTIVE SUMMARY

This report presents the results of KPMG's review of the functions performed by the Defense Automated Printing Service (DAPS) in accordance with Section 350 of the FY99 Defense Authorization Act.

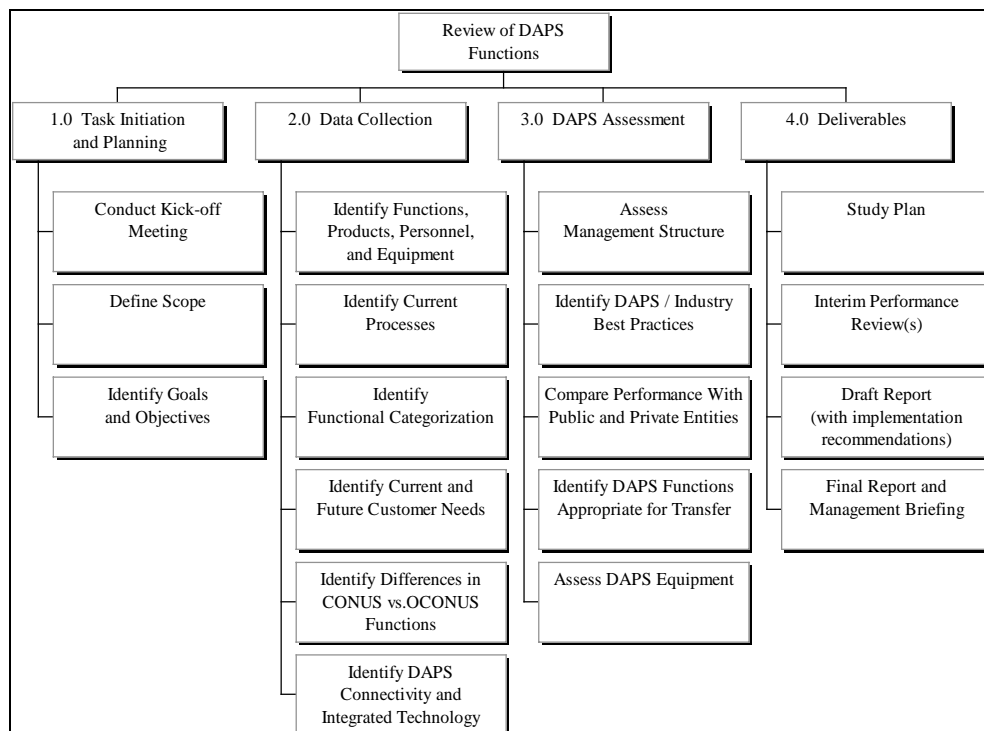
Introduction

Section 350 of the FY99 Defense Authorization Act directed the Secretary of Defense to provide for a review of the functions performed by DAPS and submit the findings of the report to the Senate Armed Services Committee and the House Committee on National Security before March 31, 1999. The Defense Logistics Agency (DLA) was delegated the responsibility for the study of DAPS and selected KPMG to perform the analytical section of the study. KPMG performed the study in consultation with the printing industry and other organizations who have experience in the printing industry.

Methodology

KPMG held a kick-off meeting with the DLA-sponsored Executive Steering Group to ensure a common understanding of the objectives, scope, and approach and establish the foundation for the scheduled tasks and proposed deliverables. Exhibit 1-1 depicts the Work Breakdown Structure (WBS) established at the commencement of the task.

Exhibit 1-1, DAPS Functional Review Work Breakdown Structure

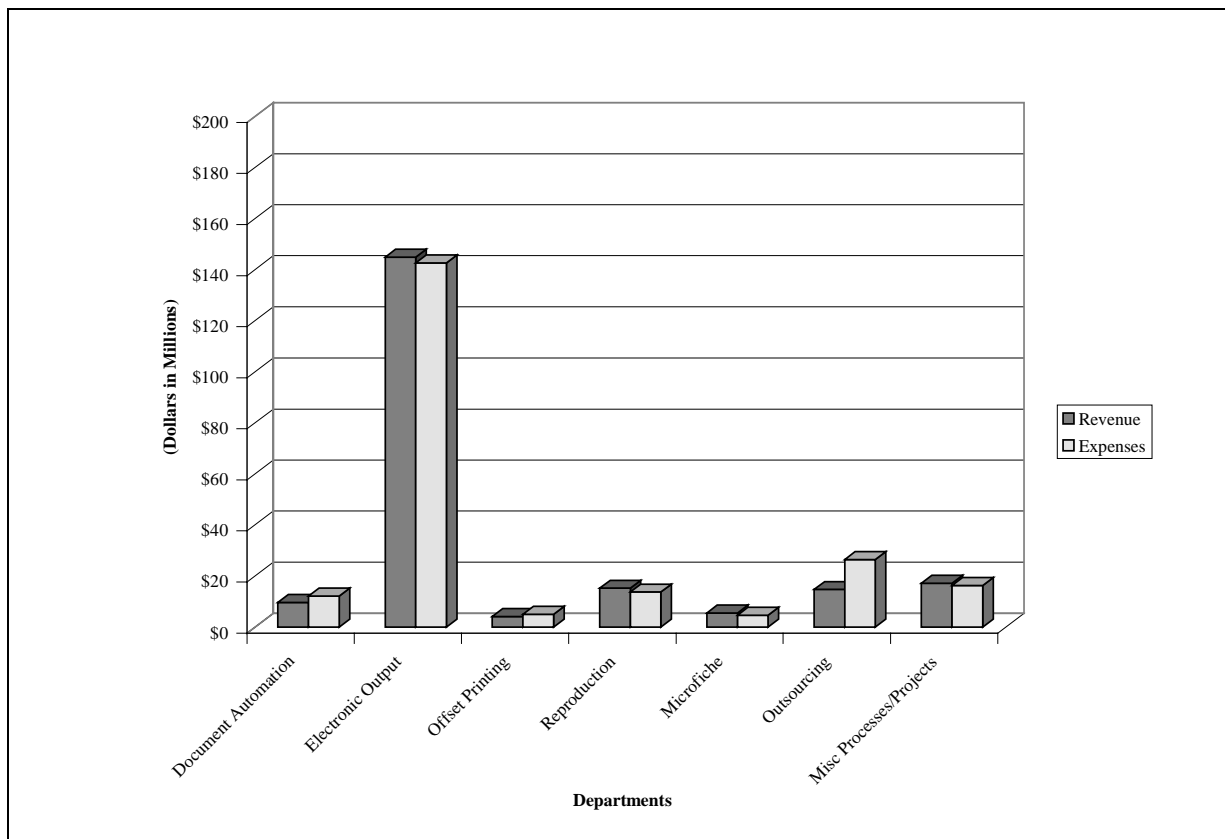


DAPS Overview

DAPS, a DLA component, is responsible for providing printing, reproduction, and document automation services to the DoD. DAPS consists of over 300 locations in 14 countries and United States territories plus a headquarters component. DAPS FY98 total revenue was \$378 Million and total expenses were \$387 Million for an overall loss of \$9 Million. \$4.5 Million of this loss is due to the mid-year implementation of Public Law 105-85 which mandated that DAPS not charge its customers a surcharge for acting as a conduit to the Government Printing Office (GPO) for jobs outsourced through GPO to commercial printers.

Exhibit 1-2 depicts DAPS FY98 revenue and expenses after adjustments were made for “pass through” revenue and expenses associated with outsourcing of work through the GPO and copier and multifunctional device contract management. A further explanation of these adjustments can be found in Section 4 of this report.

Exhibit 1-2, DAPS FY98 Revenue & Expenses by Department (without “pass through”)



Analysis

KPMG used a three step process to identify DAPS functions which may be appropriate for transfer. The three step process first involved identifying DAPS functions that meet the criteria

for “national security” and therefore must be retained in-house. Second was an assessment of whether the capability exists in the public or private sector to perform DAPS-like functions. Finally, for those functions that were determined not to be “national security” and are capable of being performed by other public or private entities, an assessment as to whether the entities could perform DAPS functions at or below DAPS costs with comparable quality and timeliness was made.

Functional Categorization

Based on the requirement levied in Section 350 of the Defense Authorization Act for FY99, the definition of national security provided in the Statement of Work, and through interviews with DAPS personnel and site visits to DAPS locations performed, KPMG concludes that there are no functions performed by DAPS which constitute “national security” functions and which must be performed by a “government controlled source.”

Industry Capabilities

The second step in the decision process is determining whether the capabilities exist in other public or private entities to perform DAPS-like functions. KPMG accomplished this assessment through industry and public entity site visits and surveys. KPMG found that industry currently performs the vast majority of DAPS-like functions.

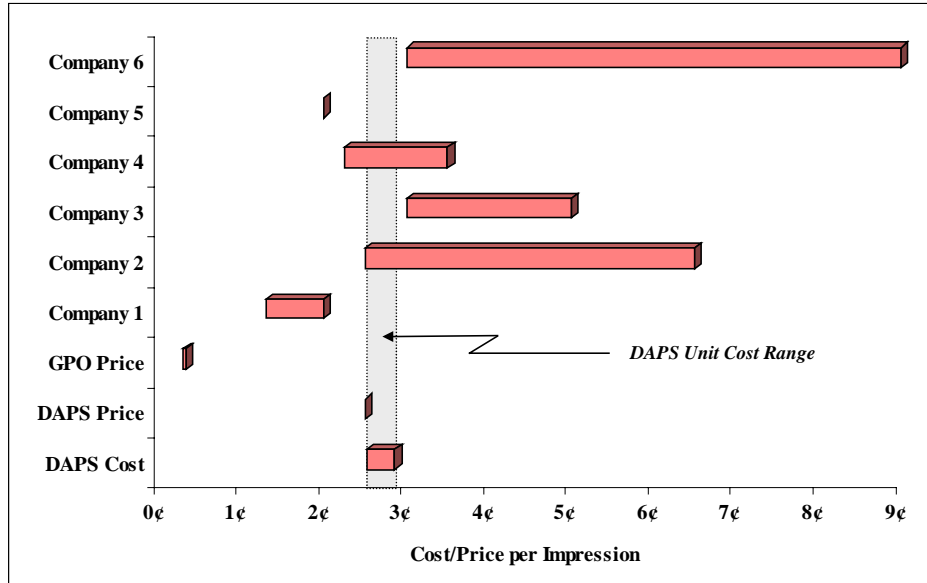
Comparison of DAPS with Other Public and Private Entities

To gather the data necessary to support a comparison with DAPS, KPMG developed a survey to be completed by the Government and commercial printing entities. The survey concentrated on large, national companies whose primary focus was electronic output. The Electronic Output department of DAPS was chosen as the primary comparison point as this function comprises nearly two-thirds of DAPS in-house business.

Using a database of 280,000 DAPS jobs completed during FY98, KPMG determined that small volume jobs (jobs requiring production of less than 10,000 impressions) represented roughly 245,000 of the 280,000 jobs in the database with large volume jobs (jobs requiring production of more than 10,000 impressions) making up the remaining 35,000 jobs. Despite constituting nearly 88% of DAPS printing jobs, these small volume jobs represented only 18% of DAPS total impressions.

Using the unit cost range derived in the report and the results of the surveys submitted by GPO and commercial entities, the following exhibits graphically display the results of the survey for small and large volume electronic output. Exhibit 1-3 compares DAPS per impression unit cost range and unit price with the small volume per impression price ranges submitted by the survey participants.

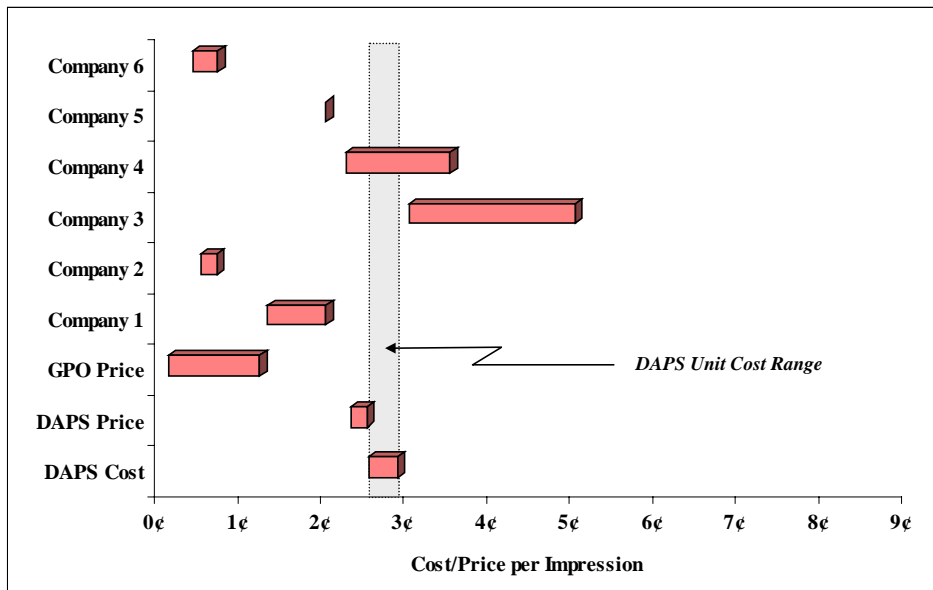
Exhibit 1-3, Comparison of DAPS per Impression Unit Cost Range and Price with Other Entities' Small Volume Prices*



** Represents 18% of DAPS Total Impressions*

Exhibit 1-4 compares DAPS per impression unit cost range and unit price range with the large volume price ranges submitted by the survey participants.

Exhibit 1-4, Comparison of DAPS per Impression Unit Cost Range and Prices with Other Entities' Large Volume Prices*



** Represents 82% of DAPS Total Impressions*

These exhibits illustrate that DAPS unit cost range is competitive with, and in several cases is lower than, other entities in small volume output. However, in large volume output, which represents over 80% of DAPS total impressions, most of the survey participants provided prices which were well below DAPS unit cost range.

Based on the data provided by industry through the private / public entity survey as well as on-site interviews with several of the respondents, KPMG concludes that the Electronic Output function may be appropriate for transfer.

Remaining DAPS Functions

Since Electronic Output represents nearly two-thirds of DAPS in-house business and has been determined to be appropriate for transfer, DAPS would have to dramatically transform operations to continue performing their remaining six functions. DAPS Financial Management Summary for FY98 indicates that these functions suffered a loss of nearly \$7 Million in FY98. Data for FY95 through FY97 also indicated losses in these functions. KPMG's interviews with industry entities indicate that all of DAPS non-electronic output functions could be performed by other entities.

Due to the apparent unprofitability of these functions, the ability of industry to perform the functions, and since DAPS in-house revenue would be reduced to roughly \$70 Million (spread over some portion of DAPS 300+ sites) without Electronic Output, these functions may be appropriate for transfer to another entity.

Conclusion

KPMG found no functions performed by DAPS that fall under the definition of "national security." In addition, based on interviews and site visits with commercial and governmental entities and the results of the private / public entity survey, KPMG believes that the capability to perform DAPS functions exists outside of DAPS. The results of surveying industry and other Government organizations has also shown that commercial or governmental entities can perform DAPS primary functions at or below DAPS costs with comparable quality and timeliness. KPMG therefore concluded that all functions performed by DAPS are appropriate for transfer and has estimated a rough order of magnitude savings of between \$28 Million and \$35 Million per year if DAPS functions are transferred to another entity although implementation costs would reduce these savings.